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JAN 6 1984
ALEXANDER L. STEVAS,
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No. 83-763

In the Supreme Court of the United States

OCTOBER TERM, 1983

ST. FRANCIS HOSPITAL CENTER, ET AL., PETITIONERS

v.

MARGARET M. HECKLER, SECRETARY,
DEPARTMENT OF HEALTH AND HUMAN SERVICES, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

MEMORANDUM FOR THE RESPONDENTS IN OPPOSITION

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Petitioners, nonproprietary hospitals that participate in the Medicare program, 42 U.S.C. (& Supp. V) 1395 *et seq.*, contend that the Secretary's denial of their claims for a return on equity constitutes a taking of their property without just compensation, in violation of the Fifth Amendment.[1]

1. This case involves Part A of the Medicare program, 42 U.S.C. (& Supp. V) 1395c *et seq.* Under Part A, a hospital (or other defined provider) is reimbursed for the "reasonable cost" of providing services to a qualified individual. 42 U.S.C. (Supp. V) 1395f(b). The Medicare statute provides

[1]Petitioners' principal claim in the lower courts was that the Medicare statute entitled them to a return on equity. They have abandoned that contention here and rely solely on their constitutional argument.

that the regulations defining reasonable costs "in the case of extended care services furnished by *proprietary* facilities shall include provision for specific recognition of a reasonable return on equity capital, including necessary working capital, invested in the facility and used in the furnishing of such services, in lieu of other allowances to the extent that they reflect similar items." 42 U.S.C. 1395x(v)(1)(B) (emphasis added). There is no comparable provision for return on equity for nonproprietary providers.[2]

Notwithstanding their nonproprietary status, petitioners claimed reimbursement on their cost reports for fiscal years ending in 1977 and 1978 for a return on net capital used in providing services to Medicare patients ("return on equity"). Petitioners' intermediary, Blue Cross of Indiana, denied the claims. Petitioners appealed that decision to the Provider

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[2]The Secretary's regulations expand on the distinction between proprietary providers, which are afforded a return on equity capital, and nonproprietary providers, which are not (42 C.F.R. 405.429):

> **Return on equity capital of proprietary providers.**
>
> (a) *Principle.* (1) A reasonable return on equity capital invested and used in the provision of patient care is allowable as an element of the reasonable cost of covered services furnished to beneficiaries by proprietary providers. * * *
>
> (2) For the purposes of this subpart, the term "proprietary providers" is intended to distinguish providers, whether sole proprietorships, partnerships, or corporations, that are organized and operated with the expectation of earning profit for the owners, from other providers that are organized and operated on a nonprofit basis.
>
> (b) *Application*—(1) *Computation of equity capital.* Proprietary providers generally do not receive public contributions and assistance of Federal and other governmental programs in financing capital expenditures. Proprietary institutions historically have financed capital expenditures through funds invested by owners in the expectation of earning a return. A return on investment, therefore, is needed to avoid withdrawal of capital and to attract additional capital needed for expansion. * * *

Reimbursement Review Board (PRRB), which found that petitioners' claims set forth reasonable costs for which they were entitled to reimbursement under the Medicare program (Pet. App. A104-A135). The Deputy Administrator of the Health Care Financing Administration, acting on behalf of the Secretary of Health and Human Services, thereafter reversed the PRRB's decision and denied reimbursement (*id.* at A76-A103). Petitioners then filed this action in the United States District Court for the Southern District of Indiana.

On cross motions for summary judgment, the district court affirmed the decision of the Secretary (Pet. App. A33-A75; 544 F. Supp. 1167). Based on both the language of the statute and the legislative history, the district court held first that Congress did not intend to permit nonproprietary hospitals to claim reimbursement for return on equity (Pet. App. A60-A67). The court explained (*id.* at A60) that "[t]he rationale for the distinction [between proprietary and nonproprietary hospitals] is that proprietary providers must raise capital through funds invested by owners in the expectation of earning a profit. Alternatively, nonproprietary hospitals have other sources of funding, i.e., public contributions and governmental programs." The district court also rejected petitioners' claim that the Secretary's denial of reimbursement constituted a taking of private property without just compensation (*id.* at A68-A71).

The court of appeals affirmed, incorporating by reference the relevant portions of the district court's opinion (Pet. App. A1-A32; 714 F.2d 872). In addition, the court of appeals explained that petitioners' "just compensation" argument was foreclosed by the voluntary nature of their participation in the Medicare program (Pet. App. A7):

> Medicare is a federally sponsored insurance program for the aged and disabled, 42 U.S.C. § 1395c, and provider participation is voluntary, 42 U.S.C. § 1395cc.

> Providers who opt not to participate are free to serve persons not covered by Medicare and those potential Medicare recipients who are willing to forego Medicare benefits for the services provided. As a practical matter, perhaps few of those persons eligible for Medicare would choose a non-participating hospital, but the fact that practicalities may in some cases dictate participation does not make participation involuntary. Even those hospitals that have an obligation to participate in the Medicare program because of their receipt of funds under the Hill-Burton Act * * * made a voluntary choice to accept both the obligations and the benefits of Hill-Burton funding. * * * We therefore find *Smyth* v. *Ames*, [169 U.S. 466 (1898)], and its progeny to be inapposite, and conclude, with the district court, that there has been no violation of the Fifth Amendment just compensation provision.

2. The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review therefore is not warranted.

As the court of appeals observed, participation in the Medicare insurance program by health care providers like petitioners is voluntary. 42 U.S.C. (& Supp. V) 1395cc. Hospitals may decline to participate and, instead, may serve patients not covered by the Medicare program and potential recipients of Medicare benefits who are willing to forego those benefits. Because petitioners' participation in the Medicare program is the product of their own choice — and not the result of government compulsion — the Secretary's denial of reimbursement for particular costs incurred by them in providing services under the program does not constitute a "wrest[ing]" by the government of "the property of one individual * * * for the benefit of another, or of the public." *Smyth* v. *Ames*, 169 U.S. 466, 524-525 (1898). See also *Pharmacist Political Action Committee* v. *Harris*,

502 F. Supp. 1235, 1243 (D. Md. 1980) (maximum allowable cost regulations for prescription drugs dispensed under Medicare and Medicaid programs not a taking because participation in the programs is voluntary).

Petitioners rely (Pet. 7-14) on decisions of this Court holding that the government, in prescribing rates to be charged by regulated industries, cannot set the rates so low as to be confiscatory. In those cases, however, the providers' participation was "voluntary" only in the sense that they could withdraw from the affected industry and thereby not be subject to the allegedly confiscatory rates. It might well be, as petitioners argue (Pet. 14), that if such "voluntary" participation foreclosed a just compensation claim the exception would virtually swallow the rule.

By contrast, in the Medicare program the government does not mandate the charging of particular rates as to any part of the market. It merely sets a limit on the amounts it is willing to pay for specified services under a government insurance program. Providers who decline to participate in the Medicare program are entirely free to continue to offer their services, at whatever rates they choose, to any potential recipient. As the court of appeals observed (Pet. App. A7), "[a]s a practical matter, perhaps few of those persons eligible for Medicare would choose a non-participating hospital, but the fact that practicalities may in some cases dictate participation does not make participation involuntary."

Petitioners' specific reliance on *Banton* v. *Belt Line Ry.*, 268 U.S. 413 (1925), also is misplaced. In the first place, the argument of the Public Service Commission that this Court rejected in *Banton* was not that the rail line (Belt Line) was precluded from challenging the allegedly confiscatory rate because its operation of a street railway was voluntary, but rather that Belt Line had "voluntarily assumed the obligation to carry transfer passengers *pursuant to [the challenged*

rate]" (268 U.S. at 417-418) (emphasis added). Moreover, in *Banton* this Court reaffirmed its prior holdings that the Fifth Amendment's protection against confiscatory taking means only that the government "may not *compel* the use and operation of [a] company's property for public convenience without just compensation." *Id.* at 420 (emphasis added). The Court's rejection of the Commission's argument represented nothing more than a determination that Belt Line's assumption of the obligation to charge the challenged rate in that case was not voluntary. *Id.* at 418-419.[3]

By contrast, because petitioners here concededly (Pet. 5 & n. 1) have chosen to participate in the Medicare program, there has been no "wrest[ing]" away of private property that would trigger an inquiry into whether petitioners have received just compensation.

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[3]For the same reason, *Denver* v. *Denver Union Water Co.*, 246 U.S. 178 (1918) (Pet. 13), also does not support petitioners' position. In that case the Court specifically found (246 U.S. at 188) that the water company "has been and is compelled to continue to serve the City and its inhabitants with water." The fact that that obligation might not have continued in perpetuity, on which petitioners rely (Pet. 13), hardly detracted from the then-present, *mandatory* nature of the undertaking. See 246 U.S. at 191.

Finally, contrary to petitioners' assertion (Pet. 12), the denial of a return on equity to nonproprietary hospitals does not amount to subsidization of nonMedicare patients by Medicare patients. Rather, as the Deputy Administrator concluded (Pet. App. A95-A96), "if a return on equity capital were paid to non-profit hospitals, Medicare would be paying a disproportionate share of provider costs. This is because the return is a profit rather than a cost. Under Section 1861(v)(1)(A) of the Act and the supporting regulations, Medicare reimburses all of a provider's reasonable costs in caring for Medicare beneficiaries. This includes a proportionate share of the cost of capital investment related to patient care such as a building or equipment."

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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JANUARY 1984

DOJ-1984-01